STRADLEY RONON

Tax Insights

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House Ways and Means Committee Releases Tax Reform Bills

The House Ways and Means Committee, on Sept. 10, released three bills that collectively constitute the Republicans' proposal for additional tax reform measures (see the Committee's release on the bills here (https://waysandmeans.house.gov/committee-passed-tax-reform-2-0/)). The bills focus on making permanent certain provisions of the Tax Cuts and Jobs Act (TCJA). House Republicans could, however, have trouble rounding up the 216 votes needed to pass the reform measures due to the prospect of widening the federal budget deficit, which was increased by tax cuts made by the TCJA in December 2017. Ways and Means Committee Chairman Kevin Brady (R-Texas) plans to put the bills to a full House vote by Oct. 1. The bills, which were approved by the House Ways and Means Committee on Sept. 13, are as follows:

- Protecting Family and Small Business Tax Cuts Act of 2018 (https://waysandmeans.house.gov/wp-content/uploads/2018/09/20180913-AINS-to-H.R.-6760.pdf) (This act would, in part, make permanent the deduction for qualified business income; the increase in the standard deduction; the limitation on deduction for qualified residence interest; the termination of miscellaneous itemized deductions; and the increased alternative minimum tax exemption for individuals.)

- Family Savings Act of 2018 (https://waysandmeans.house.gov/wp-content/uploads/2018/09/20180913-AINS-to-H.R.-6757.pdf) (This act would, in part, provide rules for multiple employer plans and pooled employer plans that would "allo[w] small businesses to join together to create a 401(k) plan more affordably"; repeal the maximum age for traditional IRA contributions; and exempt individuals with certain account balances from required minimum distribution rules.)

- American Innovation Act (https://waysandmeans.house.gov/wp-content/uploads/2018/09/20180913-AINS-to-H.R.-6756.pdf) (This act would simplify and expand deductions for startup and organizational expenditures under Section 195 and preserve startup net operating losses and tax credits after ownership change.)

IRS Releases Guidance on Treatment of Certain Income Under REIT Gross Income Test

The IRS issued Revenue Procedure 2018-48 (https://www.irs.gov/pub/irs-drop/rp-18-48.pdf), which provides guidance regarding how controlled foreign corporation income, foreign currency gain, global intangible low-taxed income and certain items from passive foreign investment companies are treated for purposes of determining whether a real estate investment trust (REIT) satisfies the gross income test in Section 856(c)(2). (Section references are to the Internal Revenue Code of 1986, as amended.)

IRS Practice Unit Describes Residency Determination for Treaty Purposes

The IRS Large Business and International Division (LB&I) released a practice unit (https://www.irs.gov/pub/irs-utl/tre_p_016_02_01_06.pdf) on helping examiners evaluate whether an individual is a resident of a contracting state for purposes of a tax treaty. Generally, only residents of a contracting state may claim tax treaty benefits.

IRS Adds New Issues to LB&I's Campaign Audit Strategy

LB&I has announced the approval of five additional compliance campaigns (https://www.irs.gov/businesses/irs-announces-the-identification-and-selection-of-five-large-business-and-international-compliance-campaigns-0). The additions are as follows:

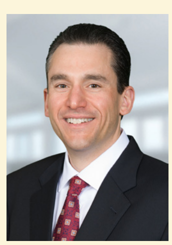
- **Former Code Section 199.** This campaign addresses all business entities that may file a claim for additional Domestic Production Activity Deductions under former Section 199 for tax years beginning after Dec. 31, 2017. The campaign objective is to ensure taxpayer compliance with the requirements of former Section 199 (which was repealed by the TCJA) through a claim risk review assessment and issue-based examinations of claims with the greatest compliance risk.

- **Syndicated conservation easement transactions.** In Notice 2017-10, 2017-4 IRB 544 (https://www.irs.gov/pub/irs-drop/n-17-10.pdf), the IRS designated specific syndicated conservation easement transactions as listed transactions, requiring disclosure statements by both investors and material advisers. This campaign is intended to encourage taxpayer compliance and ensure consistent treatment of similarly situated taxpayers by ensuring the easement contributions meet the legal requirements for a deduction and the fair market values are accurate. The initial campaign will be based on issue-based examinations, but other approaches will be considered as the campaign progresses.

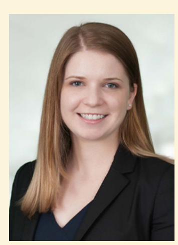
- **Foreign base company sales income: manufacturing branch rules.** The goal of this campaign is to identify and select for examination returns of U.S. shareholders of controlled foreign corporations (CFCs) that may have underreported subpart F income based on certain interpretations of the manufacturing branch rules. In general, foreign base company sales income (FBCSI) does not include income of a CFC derived in connection with the sale of personal property manufactured by such corporation. However, if a CFC manufactures property through a branch outside its country of incorporation, the manufacturing branch may be treated as a separate, wholly owned subsidiary of the CFC for purposes of computing the CFC's FBCSI, which may result in a subpart F inclusion to the U.S. shareholders of the CFC. This campaign will be based on issue-based examinations.

- **Form 1120F interest expense/home office expense.** The goal of this campaign is to increase taxpayer compliance with the interest expense rules of Treasury Regulation Section 1.882-5 (which provides a formula to determine the interest expense of a foreign corporation that is allocable to its effectively connected income) and the home office expense allocation rules of Treasury Regulation Section 1.861-8 (which governs the amount of home office expense deductions allocated to effectively connected income). The campaign includes the identification of aggressive positions in these areas, such as the use of apportionment factors that may not attribute the proper amount of expenses to the calculation of effectively connected income. This campaign will be based on issue-based examinations.

- **Individuals employed by foreign governments and international organizations.** Foreign embassies, foreign consular offices and international organizations operating in the U.S. are not required to withhold federal income and Social Security taxes from their employees' compensation, nor are they required to file information reports with the IRS. This lack of withholding and reporting results in unreported income, erroneous deductions and credits, and failure to pay income and Social Security taxes. This campaign will focus on outreach and education by partnering with the Department of State's Office of Foreign Missions to inform employees of foreign embassies, consular offices and international organizations. The IRS will also address noncompliance in this area by issuing soft letters and conducting examinations.



Christopher C. Scarpa



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